



USAID | MOLDOVA

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To: All USAID Contractors and Recipients in Moldova

From: Steve Allen, Regional Legal Advisor *Stephen C. Allen*
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Subject: Revised Policy on Registration of Implementing Organizations, and Withholding and Payment of Income and Social Taxes on Local Moldovan Employees, under Moldovan Law

This letter summarizes the results of several discussions among our implementing partners and USAID, and among USAID staff, in March, 2007, and provides a revised policy on ways that our implementing organizations may best comply with various provisions of Moldovan law. This policy is meant to be hortatory rather than mandatory; we recognize that our partners must make their own decisions about how to arrange their legal affairs in Moldova, and that many have operated in Moldova successfully for many years, under a variety of arrangements.

Background: The 1994 Bilateral Agreement on humanitarian and technical economic assistance between the Moldovan and U.S. governments provides a framework for assistance, and several tax exemptions for import of project goods and for income taxes on U.S. organizations and their expatriate employees. However, the Bilateral does not provide exemptions from income or social taxes on the salaries of local Moldovan employees.

The Bilateral also does not prescribe any particular rules on how U.S. or foreign organizations should register or operate in Moldova. Hence Moldovan law is our guide with respect to corporate formation and operation. USAID encourages our implementing partners to comply with Moldovan law, unless doing so would contravene applicable U.S. law, regulations, or grant or contract provisions.

Moldovan law does not have any special provisions dealing with legal status and registration of foreign organizations involved **solely** in foreign assistance. Instead, there are separate Moldovan legal procedures for registration of commercial organizations, charitable organizations, funds, institutions or other types of legal entities.

Depending on their legal status in Moldova, USAID's implementing organizations funded by USAID can be classified in three main categories: 1) **fully registered organizations** - that have registration certificates obtained from the relevant Moldovan authority; 2) **quasi-registered organizations** – that operate in Moldova using corporate bank accounts but without securing all the elements of corporate status and 3) **organizations operating on *de facto* basis**, without formal registration.

Several U.S. organizations have recently registered themselves as representative offices of foreign companies without great difficulty, and are generally complying with local labor and tax laws. These organizations operate through corporate bank accounts, hire and fire Moldovan employees in full compliance with local labor law, pay the employer's contributions to pension and other social funds and withhold income tax and other mandatory deductions from the salaries of local employees.

The advantages of being registered (under this “new system”) is that implementing organization operates in full compliance with Moldovan laws on corporate formation, employment and taxation, and therefore will be less vulnerable to claims by the GoM authorities for back taxes on the salaries of local staff. The disadvantage is that paying the employer's portion of social taxes on local employees [“social taxes” in this letter means any and all contributions that employer and local employees are required to make to the state pension funds, mandatory medical insurance or other social programs; the social taxes' rates are reviewed and may change annually] will increase budget expenditures for salaries of local employees (about 27.5 % of local payroll).

Many USAID implementing partners, with USAID's knowledge and consent, have operated without full registration as a legal entity under Moldovan law, but instead relying on USAID's quarterly notification to the Ministry of Economy that a particular organization is implementing a specified project, plus a “fiscal code” received from the GoM tax authorities. Under this “old system”, our partners usually operated out of personal, rather than corporate bank accounts, and did not withhold nor pay income or social taxes [neither employer's nor employee's contributions]. The advantage was saving the costs of the employer's portion of social taxes. The disadvantages are continued potential liability under local law for these back taxes, and difficulties operating corporate bank accounts.

Conclusion--USAID's New Policy: After considering the advantages and disadvantages of the “new” and the “old” systems, the Regional USAID Mission has changed our policy. We now recommend and encourage our implementing partners in Moldova to follow the guidance below in order to better comply with the relevant provisions of Moldovan law, so as to minimize the possibility of future local legal problems for your organization.

- 1) New or relatively new implementing organizations are encouraged to register their

presence in Moldova in accordance with Moldovan corporate formation law. In general, steps would include obtaining a corporate registration certificate (its number serves as a fiscal code), registration as an employer to pay social tax contributions, obtaining an official seal and opening a corporate bank account. Project budgets should be revised to reflect payment of the employer's portion of social taxes, and arrangements should be made to withhold and pay the employee's portion of social and income taxes to the Moldovan tax authorities. The RCO letter dated February 28, 2005 is superseded in this regard by this letter. Any necessary adjustments in the project budget in your contract, grant or cooperative agreement will be addressed in a future modification, as needed.

- 2) Implementing organizations whose projects will end by December 31, 2007, should to operate the same way as they have, and need not change their methods of operations.
- 3) Existing implementing organizations whose projects will not end by December 31, 2007 and who are not fully registered, are also encouraged to register their presence in Moldova in accordance with local corporate formation laws, and to follow the "new system" as described in 1) above.

Please send your questions about these topics first to your Cognizant Technical Officer, who will forward them within USAID for discussion and response.